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Message Text

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ACTION ARA-14

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-08 FRB-03
INR-10 NSAE-00 ICA-11 TRSE-00 XMB-02 OPIC-03
SP-02 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-07
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E.O. 11652: N/A
TAGS: ETRD, EFIN, JM
SUBJECT: EVALUATION OF JAMAICA'S IMPORT LICENSING AND FOREIGN EXCHANGE CONTROL SYSTEM

REFERENCE: A. STATE 061741 B. 77 KINGSTON 7075 C. KINGSTON 0411 D. KINGSTON 0295

1. SUMMARY: COMPLAINTS FROM THE PRIVATE SECTOR SUGGEST THAT JAMAICA'S IMPORT LICENSING AND FOREIGN EXCHANGE CONTROL SYSTEMS ARE NOT WORKING WELL. CERTAINLY, THE COUNTRY'S SERIOUS BALANCE OF PAYMENTS SITUATION WOULD HAVE PLACED SEVERE CONSTRAINTS ON INCOME, GROWTH AND EMPLOYMENT UNDER ANY SYSTEM. HOWEVER, THERE ARE INDICATIONS THAT THE EXCHANGE CONTROL SYSTEM PRESENTLY IN FORCE MAY BE FURTHER EXACERBATING THE PROBLEM BY MAKING IT DIFFICULT FOR FACTORIES AND BUSINESSES TO OBTAIN A CONTINUOUS FLOW OF ESSENTIAL RAW MATERIALS AND PARTS, DISCOURAGING INVESTMENT, UNDERMINING CONFIDENCE, STIMULATING CAPITAL FLIGHT AND DIVERTING FOREIGN EXCHANGE SUPPLIES TO THE BLACK MARKET. CURRENT LIMITED OFFICIAL USE

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POLICIES MAY ENDANGER THE CONTINUED AVAILABILITY OF ESSENTIAL GOODS AND SERVICES SUCH AS PETROLEUM AND SERVICING BY INTERNATIONAL AIRLINES. MEASURES SHOULD BE ADOPTED AS SOON AS POSSIBLE TO ELIMINATE THE MANY DISEQUILIBRIA IN THE JAMAICAN ECONOMY AND RESTORE THE CONFIDENCE OF THE PRIVATE SECTOR. (END SUMMARY)

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2. SPOKESMEN FOR THE JAMAICA CHAMBER OF COMMERCE AND THE JAMAICA MANUFACTURERS' ASSOCIATION RECENTLY DISCUSSED WITH EMBASSY OFFICERS THE SERIOUS IMPACT THAT THE PRESENT FOREIGN EXCHANGE CRISIS, AGGRAVATED BY THE MALFUNCTIONING OF THE FOREIGN EXCHANGE CONTROL MACHINERY, WAS HAVING ON THE ECONOMY. RAW MATERIALS AND ESSENTIAL SPARE PARTS HAVE BEEN ACCUMULATING ON THE WHARVES FOR SEVERAL WEEKS AND BUSINESSMEN HAVE NOT BEEN ABLE TO GET THEM RELEASED. IMPORT LICENCES FOR ALL OF THESE MATERIALS AND PARTS HAVE BEEN DULY OBTAINED, LETTERS OF CREDIT OR SIGHT DRAFTS ISSUED AND, IN MANY CASES, APPROVAL FROM THE BANK OF JAMAICA OBTAINED. YET, THE COMMERCIAL BANKS WILL NOT PROVIDE THE FUNDS AS LONG AS THE OBLIGATIONS HAVE NOT BEEN ACTUALLY COVERED BY THE BOJ, WHICH IS SO SHORT OF FUNDS THAT IT IS UNABLE TO COVER ITS OBLIGATIONS.

3. PRACTICALLY ALL MANUFACTURING INDUSTRIES ARE AFFECTED, INCLUDING TEXTILES, GARMENTS, FOOTWEAR, AUTO PARTS, METAL INDUSTRIES, FURNITURE AND MATCHES, TO NAME A FEW. AUTOMOBILE PARTS DEALERS CALLED ON THE TRADE ADMINISTRATOR TO STOP ISSUING LICENCES TO IMPORTERS WHEN NO FOREIGN EXCHANGE WAS AVAILABLE TO PAY FOR THEM. "IT IS BETTER FOR US TO BE TOLD THE TRUTH SO THAT WE CAN COOPERATE WITH THE TRADE ADMINISTRATOR THAN FOR US TO BE GRANTED LICENCES AND WHEN THE TIME COMES TO PAY THE LIMITED OFFICIAL USE

SUPPLIERS, THERE IS NO FOREIGN EXCHANGE", DECLARED THE SECRETARY OF THE JAMAICA AUTO PARTS DEALERS ASSOCIATION.

4. A NUMBER OF JAMAICAN BUSINESSMEN WITH AN ESTABLISHED REPUTATION HAVE TRADITIONALLY IMPORTED THEIR GOODS ON OPEN ACCOUNT. IN RECENT MONTHS, HOWEVER, SIGHT DRAFTS COULD NOT BE HONORED. U.S. EXPORTERS THEN DEMANDED OPENING OF LETTERS OF CREDIT PRIOR TO SHIPMENT. NOW, COMMERCIAL BANKS ARE REFUSING TO ISSUE LETTERS OF CREDIT BECAUSE THEY CANNOT COLLECT THE NECESSARY FOREIGN EXCHANGE FROM THE BOJ. THIS NOT ONLY SERIOUSLY DISRUPTS THE NORMAL COURSE OF TRADE AND ECONOMIC ACTIVITY, BUT UNDERMINES THE COUNTRY'S CREDIT STANDING.

5. MANY BUSINESSES HAVE BEEN FORCED TO FOLD OR CURTAIL OPERATIONS AND DISCHARGE PART OF THEIR WORK FORCE. THE PRESIDENT OF THE JAMAICA MANUFACTURERS' ASSOCIATION ESTIMATED THAT MANUFACTURING INDUSTRY IN GENERAL WAS OPERATING AT ONLY 45-50 PERCENT OF CAPACITY.

6. ADDITIONAL EVIDENCE OF DISRUPTION IS PROVIDED BY THE DIFFICULTY THAT CERTAIN KEY INDUSTRIES ARE

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EXPERIENCING IN CONVERTING THEIR ACCUMULATED STOCKS OF
JAMAICAN DOLLARS INTO FOREIGN EXCHANGE. THE FOUR
INTERNATIONAL AIRLINES OPERATING IN JAMAICA HAVE BEEN
USED BY JAMAICAN RESIDENTS AS INSTRUMENTS FOR THE
EXPATRIATION OF CAPITAL THROUGH SUCH DEVICES AS
PURCHASING ROUND-TRIP TICKETS FOR FRIENDS AND RELATIVES
RESIDING ABROAD AS WELL AS BUYING ROUND-THE-WORLD
TICKETS THAT ARE THEN RE-ISSUED ABROAD AND CONVERTED,
THROUGH REFUNDS, INTO FOREIGN EXCHANGE. THE AIRLINES
HAVE CURRENTLY ACCUMULATED $8-10 MILLION IN JAMAICAN
CURRENCY THAT THEY CANNOT CONVERT INTO DOLLARS, EVEN
THOUGH SUCH CONVERSION IS GUARANTEED BY THEIR
AGREEMENTS WITH THE GOVERNMENT. ESSO HAS ACCUMULATED
A FROZEN CREDIT BALANCE OF $14 MILLION (REF A). UNLESS
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THE FOREIGN EXCHANGE FOR THE REIMBURSEMENT IS SOMEHOW
FOUND IN THE COMING MONTHS, THERE IS THE POSSIBILITY
THAT THE SUPPLY OF ESSENTIAL SERVICES AND FUEL WILL BE
CUT OFF, OR AT LEAST INTERRUPTED.

7. THE COUNTRY WOULD FACE A SERIOUS BALANCE OF PAYMENTS
PROBLEM AND THE NEED TO REDUCE ITS STANDARD OF LIVING UNDER
ANY KING OF FOREIGN EXCHANGE SYSTEM. ITS OVERALL BALANCE
OF PAYMENTS DEFICIT WAS $265 MILLION IN 1976 AND $43
MILLION IN 1977. THE CAUSES OF ITS BALANCE OF PAYMENTS
PROBLEM ARE MANY AND COMPLEX (SEE ANALYSIS IN REF B AND C).
THERE ARE INDICATIONS, HOWEVER, THAT THE CURRENT IMPORT LICENSING
AND EXCHANGE CONTROL SYSTEMS FURTHER EXACERBATE THE SHORTAGE
OF FOREIGN EXCHANGE BY REDUCING OUTPUT AND EXPORTS; DISCOURAGING
FOREIGN INVESTMENT; ENCOURAGING CAPITAL FLIGHT AS FOLDING
BUSINESSES ATTEMPT TO EXPATRIATE THEIR REMAINING CAPITAL,
AND AS BUSINESSES THAT ARE STILL PROFITABLE ANTICIPATE EVEN
MORE STRINGENT MEASURES IN THE FUTURE. MOREOVER, THERE IS
EVIDENCE THAT THERE HAS BEEN AN INCREASING DIVERSION OF
FOREIGN EXCHANGE FROM OFFICIAL TO BLACK MARKET CHANNELS.
THE BLACK MARKET RATE OF ABOUT J$2.50 TO US$1.00 HAS LED TO
A SUBSTANTIAL LOSS OF TOURISM DOLLARS TO THE MONETARY AUTHORI-
TIES (REF D); WHILE MORE AND MORE JAMAICANS LIVING ABORAD
ARE PAYING THEIR REMITTANCES INTO FOREIGN BANK ACCOUNTS.

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R 071800Z APR 78
FM AMEMBASSY KINGSTON
TO SECSTATE WASHDC 0585
INFO AMEMBASSY CARACAS
AMEMBASSY GEORGETOWN

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8. BUSINESSMEN DO NOT QUESTION THE NEED TO CUT BACK ON THE USE OF FOREIGN EXCHANGE. HOWEVER, THEY ARE HIGHLY CRITICAL OF THE SYSTEM CURRENTLY IN FORCE. THEY BELIEVE THAT THE TRADE ADMINISTRATOR'S STAFF DOES NOT HAVE THE TECHNICAL COMPETENCE TO ASSIGN PRIORITIES AND THAT DECISIONS ON ALLOCATIONS ARE MADE WITHOUT CONSULTING THE BUSINESS SECTORS INVOLVED. THEY RESENT THE DISBANDMENT OF ADVISORY COMMITTEES THAT FUNCTIONED IN PREVIOUS YEARS AND COMPLAIN THAT THE AMOUNT OF INFORMATION THAT MUST BE SUPPLIED TO SUPPORT EVERY APPLICATION FOR AN IMPORT LICENSE PLACES A HEAVY BURDEN ON THE APPLICANTS. IT IS CLAIMED THAT SOME OF THE INFORMATION CALLED FOR IS BEYOND THE CAPACITY OF THE BUSINESSES TO PROVIDE.

9. SEVERAL FACTORS OTHER THAN THE MANAGEMENT OF FOREIGN EXCHANGE RESERVES CONTRIBUTE TO THE MALAISE OF THE PRIVATE SECTOR. BUSINESSMEN PLACE PARTICULAR EMPHASIS ON THE "PUNITIVE" HEIGHT OF THE RATES OF THE PERSONAL INCOME TAX - 70 PERCENT ON THE J$20,000 TO J$30,000 ANNUAL TAXABLE INCOME RANGE, AND 80 PERCENT ON THE EXCESS OVER J$30,000 - WHICH SERIOUSLY INTERFERE WITH ECONOMIC INCENTIVES. OTHER FACTORS MENTIONED
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INCLUDE THE GOVERNMENT'S RHETORIC AND APPREHENSION WITH RESPECT TO FUTURE GOVERNMENT ACTION.

10. THE TRADE ADMINISTRATOR ADMITS THAT A NUMBER OF IMPORT LICENSES WERE ISSUED LAST YEAR WITHOUT THE REQUISITE FOREIGN EXCHANGE COVER. THE LICENCES WERE ISSUED ON THE BASIS OF PROJECTED FOREIGN EXCHANGE INFLOWS WHICH APPEARED REASONABLE AT THE TIME. UNFORTUNATELY, THE SUSPENSION OF THE IMF STAND-BY PREVENTED THE RECEIPT OF A NUMBER OF LOANS THAT

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HAD BEEN COUNTED ON - INCLUDING A $30 MILLION IBRD LOAN, $32 MILLION FROM U.S. COMMERCIAL BANKS AND THE IMF FIRST QUARTER ('78) TRANCHE ITSELF. THIS SHORT-FALL IS DIRECTLY RESPONSIBLE FOR THE ORDERING OF MATERIALS WHICH ARE NOW PILING UP ON THE DOCKS.

11. THE TRADE ADMINISTRATOR ADMITS THAT THE INTRODUCTION OF THE NEW IMPORT LICENSING SYSTEM CAUSED CONSIDERABLE DELAYS AT THE OUTSET. HOWEVER, HE FEELS THAT THE SYSTEM IS PRESENTLY WORKING WELL AND WILL IMPROVE FURTHER. DELAYS IN PROCESSING LICENSE APPLICATIONS WERE CUT BACK FROM 3-4 MONTHS INITIALLY TO TWO WEEKS NOW. THEY WILL SOON BE PROCESSED IN THE SAME WEEK THEY ARE SUBMITTED AS A RESULT OF THE COMPUTERIZATION OF ALL APPLICATIONS. HE ALSO STATED THAT ABOUT HALF OF HIS STAFF ARE TRAINED ECONOMISTS AND STATISTICIANS, WITH THE REMAINDER WELL EQUIPPED TO HANDLE THE REQUESTS. IN HIS VIEW, THE PRIVATE SECTOR LEADERSHIP WAS GENERALLY SATISFIED WITH THE SYSTEM'S OPERATION.

12. YET, THE PRIVATE SECTOR REPRESENTATIVES WE INTERVIEWED WERE STRONGLY CRITICAL, FRUSTRATED AND BITTER. IT IS THUS CLEAR THAT THERE IS A LACK OF COMMUNICATION BETWEEN THE PRIVATE SECTOR AND THE TRADE ADMINISTRATOR'S OFFICE.

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13. WHILE THERE IS ROOM FOR IMPROVEMENT OF THE CURRENT IMPORT LICENSING AND IMPORT CONTROL SYSTEMS, WE DOUBT THAT THE OVERALL SITUATION WILL BE MUCH IMPROVED EVEN IF THEY COULD BE MADE TO FUNCTION MORE EFFECTIVELY. THERE IS AN URGENT NEED FOR A BASIC CHANGE IN THE GOVERNMENT'S MACRO-ECONOMIC POLICIES. SPECIFICALLY, BUDGETARY DEFICITS NEED TO BE CURBED: THESE INCREASED FROM J$53 MILLION IN 1972 TO J$677 MILLION IN 1977. THE TAX STRUCTURE SHOULD BE REVISED TO MAINTAIN ECONOMIC INCENTIVES; THE GROWTH OF MONEY SUPPLY AND WAGE RATES MUST BE CHECKED TO RESTORE A BETTER BALANCE BETWEEN THE GROWTH OF PRODUCTIVITY AND INCOMES; EXCHANGE RATES SHOULD BE UNIFIED AND FURTHER DEVAULED; FOREIGN EXCHANGE AND TRADE CONTROLS SHOULD BE LIBERALIZED; AND A COMPREHENSIVE PROGRAM SHOULD BE ADOPTED TO RESTORE THE CONFIDENCE OF THE PRIVATE SECTOR (BOTH JAMAICAN AND FOREIGN) AND CONVERT THE OUTFLOW OF PRIVATE CAPITAL INTO THE NET INFLOW THAT, HISTORICALLY, PREVAILED EVERY YEAR THROUGH 1975.

14. MINISTER OF STATE FOR PLANNING RICHARD FLETCHER EXPLAINED THAT ADOPTION OF SOME OF THE CORRECTIVE MEASURES NOTED ABOVE IS VERY DIFFICULT POLITICALLY. IN PARTICULAR, IT IS FEARED THAT EXCHANGE RATE FLOATS OR DEVALUATION WOULD GIVE RISE TO STRONG UNION DEMANDS FOR

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PROPORTIONAL WAGE INCREASES THAT THE GOVERNMENT WOULD NOT HAVE TO POWER TO RESIT. THE RESULT COULD BE INFLATION WITHOUT IMPROVEMENT IN THE BALANCE OF PAYMENTS POSITION. MOREOVER, THE GOVERNMENT IS MOST RELUCTANT TO ALLOW THE PRICE OF FOREIGN EXCHANGE TO PERFORM THE RATIONING FUNCTION, GIVEN THE EXISTING MALDISTRIBUTION OF INCOMES.

15. CENTRAL BANK OFFICIALS STRESS THAT THE RELAXATION OF EXCHANGE CONTROLS IS ONLY POSSIBLE IF THE COUNTRY GAINS ACCESS TO A CUSHION OF FOREIGN EXCHANGE RESERVES TO MEET THE CLAIMS THAT, IN THEIR VIEW, WOULD FOLLOW THE LIMITED OFFICIAL USE

ELIMINATION OF CONTROLS. WHILE IT CAN BE ARGUED THAT THE DEMAND FOR FOREIGN EXCHANGE IS MORE LIKELY TO FALL THAN TO RISE IF CONTROLS ARE ELIMINATED AND THE EXCHANGE RATE IS PERMITTED TO SEEK ITS OWN LEVEL, IT IS CLEAR THAT THE JAMAICAN AUTHORITIES WOULD NOT RISK REMOVING CONTROLS UNLESS THEY HAD A FOREIGN EXCHANGE CUSHION TO MEET THE UPSURGE IN DEMAND THAT THEY EXPECT. NO MATTER HOW UNPALATABLE OR POLITICALLY DIFFICULT, IT WOULD SEEM THAT THE MEASURES DESCRIBED IN PARAGRAPH 13 EVENTUALLY MUST BE ADOPTED. WHEN CLEAR EVIDENCE IS PROVIDED THAT THEY WILL BE, IT IS HOPED THAT THE IMF AND OTHERS DONORS WILL BE READY TO PROVIDE THE FOREIGN EXCHANGE RESOURCES REQUIRED TO TIDE THE COUNTRY OVER WHILE THE CORRECTIVE MEASURES TAKE EFFECT.
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